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Maylie & Grayson is a full service law firm providing representation to real estate brokerages, licensees, Realtor® associations, developers, builders, lenders and investors, providing services in all aspects of real estate including transaction review, land use planning, licensing, mediation, arbitration and court matters throughout Oregon and Washington.

SHORT SALES UPDATE

Almost a year ago, we wrote an article regarding short sales and the plight of subprime mortgages. Unquestionably, the real estate market has changed in the last year, with some regions experiencing decreasing values, higher default rates, and higher foreclosure rates. Fortunately, the Northwest region of the country has experienced less of this than other regions. However, with the possibility that the real estate market may continue to change, and with key national legislation being passed, we thought it would be worthwhile to revisit the subject in light of recent changes in the market.

Mortgage Forgiveness Debt Relief Act of 2007

Until recently, sellers who participated in a short sale were potentially liable for a significant amount of taxes. This tax liability originated when a lender forgave a portion of the seller's debt owed on the property, allowing the seller to sell his or her property for less than what may have been owed. In essence, the IRS treated this forgiven debt as income, and the seller was liable to the IRS for the tax on that additional income.

Unfortunately, many sellers may not have had the financial wherewithal to pay tax on that invisible income, since those sellers may have already been in a financial bind. Recognizing this predicament, the federal government passed legislation in December 2007 which alleviates financial stress put on homeowners who may be struggling to satisfy their debts. This legislation, appropriately named the Mortgage Forgiveness Debt Relief Act of 2007, revises a section of the Internal Revenue Code which classifies forgiven debt as income. As a result of the Act, Sellers will not be taxed on up to \$2,000,000 of debt (\$1,000,000 if filing individually) that is forgiven upon sale of the sellers' principal residences. The Act is retroactive, in that it applies to debt forgiven on or after January 1, 2007, and will be in effect until January 1, 2010.

Although we do not encourage real estate licensees to give their clients tax advice, we believe licensees should be armed with knowledge, thereby providing better service to their clients. Licensees may provide general information, but would be wise to advise their clients to seek specific information from CPAs or other tax advisors.

Short Sale Experts

For many licensees, short sales may be unfamiliar territory, as short sales tend to be less common in a boom market. In addition, licensees may not be as inclined to provide representation in short sales when there are plenty of other opportunities available in the market. As many licensees may know, short sales may involve more work and potentially less pay. However, in a slowing market, many licensees may decide to challenge themselves by delving into unfamiliar territory.

Licensees have undoubtedly heard of other licensees or companies, located locally or out of state, that are holding themselves out as “short sale specialists.” In fact, a licensee listing a short sale property may be contacted by a specialist who offers to assist the licensee with negotiating debt forgiveness with the seller’s lender(s) in exchange for a portion of the licensee’s commission.

Although there is nothing inherently illegal with this business model, licensees should be aware of potential issues that may arise out of working with a specialist. First, licensees should absolutely know who they are dealing with by requesting references from a specialist and determining whether that specialist is a licensee. Second, licensees should be wary of specialists who want to purchase, or secure an option to purchase, a client’s property, as this may conflict with that client’s interests. Third, if the specialist is legitimate, licensees should consider whether their clients would consent to having a specialist assist in the transaction. Issues a licensee may want to discuss with a client include the specialist’s real estate license or lack thereof, the specialist’s background and experience, and how the specialist will be paid. Fourth, licensees should be actively involved in the specialist’s work, as ultimately, the licensee is the individual who is most at risk for violating duties and obligations to the client. The client may hold the licensee responsible for the specialist’s work.

Licensees who list short sale properties should be careful in teaming with a specialist who claims they will do most of the licensee’s work for them for only a portion of the commission. In addition, licensees should be careful in working with a specialist whose sole motivation may be to purchase or option the client’s property at a low price. It has always been important for licensees to know who they are dealing with, particularly when it comes to new business models that licensees may not understand. Licensees who believe they need assistance in listing a short sale may benefit from referring the listing to an individual who has experience rather than using the services of a specialist. In many cases, the licensee may be successful in negotiating a referral fee, without opening themselves up to liability resulting from lack of experience. When a short sale situation presents itself, licensees would be well advised to immediately review the matter with their principal brokers before proceeding.

Conclusion

As always, licensees should educate themselves on changes in the marketplace, keeping abreast of changes in laws, rules and regulations, and familiarizing themselves with different business models that may come into existence as a result of changes in the market. Such

education will pay huge dividends, with licensees providing better service to their clients and potentially having less liability for their actions.

This column contains general information only and must not be construed as legal advice. Questions may be submitted directly to Maylie & Grayson by fax at (503) 775-1765, by email at joelgrayson@mayliegrayson.com or by mail at 7959 SE Foster Road, Portland, Oregon 97206.

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